IN THE HIGH COURT OF JUDICATURE AT BOMBAY
CIVIL APPELLATE JURISDICTION

FIRST APPEAL NO. 692 OF 1989.

Mula Sahakari Sakhar Karkhana Ltd., being a Cooperative Society registered under the Maharashtra Cooperative Societies Act, 1960, and having it's Registered Office at and Post Sonai, Taluka Newasa, District Ahmednagar.	]	.. Appellant (Plaintiff)
Vs		
1. State Bank of India (Dombivli Industrial Estate Branch), at and post Dombivli Industrial Estate, District Thane.	]	
2. The State Bank of India, Regional Office V, 88/C, Leo House, Old Prabhadevi Road, P.B. 19168, Bombay.	]	.. Respondents ..(Defdt.1 & 2)

Shri Prashant Naik for the appellant.

Shri Thushar Koopar with Shri Jaychandra for the respondent.

CORAM: R.M.S. KHANDEPARKAR &
ANOOP V. MOHTA, JJ.

DATED: 2ND AUGUST, 2005

ORAL JUDGMENT: [Per Anoop V. Mohta, J.]

1. The appellant-plaintiff has preferred the present appeal against the judgment and order dated 4th February, 1989, passed by the Civil Judge, Senior Division, Ahmednagar, in Special Civil Suit No. 310 of

1987, whereby, the Suit was dismissed.

2. The appellants is a Co-operative Sugar Factory, having its registered office at Post Sonai village, Taluka Newasa, District Ahmednagar. By an agreement dated 25th September, 1983, the appellant executed the contract for erection of a paper plant at village Sonai on a turn-key basis to utilise the left over material called "bagasse" of the sugarcane with M/s. Pentagon Engineering Pvt. Ltd. (for short "M/s. Pentagon"). The total value of the contract was Rs.3,40,00,000/-. Time was the essence of the contract. The said Pentagon had guaranteed the performance as agreed. As per clause 15 to 17 of the agreement, the appellants were entitled to retain 10% of the amount and which were to be paid after 3 to 6 months after successful working of the same after it was commissioned. In view of clause 15.2.4 and 15.2.5, the appellant, while making payment against the performance invoice sent by M/s. Pentagon, used to deduct 10% value of the said invoice. This 10% amount corresponds to the amount of 5% which was referred to in clauses 15.2.4 and 15.2.5 of the agreement. However, by letter dated 6th April, 1985, Pentagon requested the appellant-plaintiffs to rescind the term about the retention of the said 10% amount. The appellant agreed to accommodate Pentagon on

a condition to submit the Bank Guarantee against the release of the amount of Rs.34,00,000/-. The correspondences in that regard is at Exhibit-47 to Exhibit-52 of the Paper Book. The document in question (Exhibit-46) was accordingly executed based on the original agreement between appellant and Pentagon dated 28/9/1983.

3. There arose disputes and differences between the appellant and M/s. Pentagon. By Notice dated 17th July, 1987, the contract was terminated by Pentagon. The appellant raised the claim by Notice in the sum of Rs.3,23,28,209.10 as set out in paragraphs 10 and 11 of the Plaint. Pentagon, however, denied the liability and claimed an amount of Rs.4,66,73,300/- vide their Advocate's letter dated 18th July, 1987 (Exhibit-53). The appellant, therefore, by letter dated 12th August, 1987 (Exhibit-57) invoked the Bank Guarantee in question.

4. The respondents, by letter dated 13th August, 1987, resisted the said demand and pointed out that at the request of Pentagon, on 4th September 1985, the respondents executed an agreement of indemnity, thereby indemnifying the appellants against all losses, claims, damages, actions and costs which may be suffered as a

result of payment of Rs.34,00,000/-. The indemnity given was only to cover the claims of the appellants against the said company. Therefore, it was pointed out that unless adjudicated that the appellants had suffered any loss or damage for design, performance, workmanship or against defective material through the competent Court or authority, and the claims, disputes and differences between the parties determined accordingly, the demand of the claim by the appellant was premature and not maintainable.

5. The appellants sent several reminders and called upon them to make the payment of Rs.34,00,000/- under the said Bank Guarantee. The appellants, therefore, on 2nd September, 1987, filed the Special Civil Suit No.310 of 1987 against the respondents before the Civil Judge, Senior Division, Ahmednagar. On 9th February, 1988, the trial Court, on an application of the appellants, directed the respondents to deposit an amount of Rs.34,00,000/-, but the said amount remained with the respondent Bank in view of the order dated 9th February, 1988, passed by the Hon’ble Court on appeal filed by the respondent-Bank with condition that the respondent-Bank should pay the amount with interest @ 12% in case appellants succeeds in the Suit. The Suit was transferred to the Additional District Judge, Thane.

The respondents filed their Written Statement dated 13th September, 1988, and resisted the claim and pleaded that unless and until the disputes get settled they are not liable to pay the said amount.

6. The appellants-plaintiffs led the evidence of four witness viz. Vinayak Vithoba Ambre, Tukaram Rajaram Raut, Anant Vasant Rane and Mohammed Ismail Patel. The respondents led evidence of one Shankar Purshottam Keskar, Bal Anant Vasaikar, Vijay Narayan Gadkari. Both the parties proved documents are exhibited on the record. The learned Judge, after considering the material, as well as, the evidence led by the parties, dismissed the appellants Suit in toto.

7. The learned Judge held that the appellants-plaintiffs proved that the Deed dated 4th September, 1985, was executed by the respondent No.1 (defendant No.1) at Sonai and was delivered to the appellant at Sonai as alleged and, therefore, the Court has jurisdiction to entertain and try the Suit; appellant failed to prove that the document executed on 4th September, 1985, by the respondent No.1 (defendant No.1) was a Bank Guarantee simplicitor for a sum of Rs.34,00,000/- in the capacity of Guarantor or Surety under Section 126 of the Contract Act; respondents

proved that they were to indemnify the plaintiffs "for the losses caused only on account of design, performance, workmanship and defective material or equipment supplied, as per the agreement between appellants (plaintiffs) and M/s. Pentagon Engineering Pvt. Ltd. and that the deed of indemnity dated 4th September, 1985, was issued by the respondent No.1 (defendant No.1) at the request of the company - M/s. Pentagon to cover final payment by the appellants (plaintiffs) to the said company"; M/s. Pentagon Engineering Pvt. Ltd. was a necessary and proper party and, therefore, the Suit was bad for non-joinder of M/s. Pentagon Engineering Pvt. Ltd.; appellants-plaintiffs failed to prove that the defendants (respondents) are liable to pay to the plaintiffs a sum of Rs.34,00,000/- on first demand or after invocation of the guarantee in question notwithstanding that any dispute between the appellants (plaintiffs) and the said company M/s. Pentagon Engineering Pvt. Ltd. exists or not and that the liability to the respondent No.1 (defendant No.1) to pay to the appellants (plaintiffs) the said amount was absolute and unconditional; the appellants (plaintiffs) failed to prove that M/s. Pentagon Engineering Pvt. Ltd. committed breaches, defaults under the agreement dated 25th September, 1983, and that M/s. Pentagon Engineering Pvt. Ltd. was liable to pay more than a

sum of Rs.34,00,000/- to the appellants (plaintiffs). The learned Judge, on this foundation, dismissed the Suit.

8. Heard the learned counsel Shri Naik for the appellant who basically contended that Exhibit-46 dated 4th September, 1985, is a duly executed unequivocal Bank Guarantee and, therefore, appellant was entitled for the amount of Rs.34,00,000/- as they had invoked the Bank Guarantee on 27th July, 1987. In absence of any ground of fraud or irretrievable injustice, the said Bank Guarantee ought to have been honoured. He has relied on the Apex Court's decision in the case of **Daewoo Motors India Ltd. Vs. Union of India & Ors.** (2003) 4, S.C.C., 690. The Court below has misconstrued and has misapplied the principle of law with regard to the Bank Guarantee by holding that the document in question is a contract of indemnity as contemplated under Section 124 of the Contract Act and not a document of Guarantee within the meaning of Section 126 of the Contract Act. He has further contended that the reading of the document in question dated 7th September, 1985 (Exhibit-46), pre and post correspondence and the evidence led in this behalf by the appellant, basically of the Officers of the Bank, proved the ingredients of the Bank Guarantee and, therefore, entitled for the

amount as claimed. He further contended that M/s. Pentagon was not a necessary party, as not concerned with and had no say in this matter.

9. The learned counsel for the respondent-Bank Shri Koopar resisted the above contentions and made his submissions in support of the impugned judgment and order. He has relied upon the Apex Court's judgment in **Hindusthan Construction Company Limited Vs. State of Bihar & Ors.**, (1999) 8, S.C.C., 436; **New India Assurance Company Ltd. Vs. Kusumanchi Kameshwara Rao & Anr.,** (1997) 9, S.C.C., 179; **Daewoo Motors Vs. Union of India & Ors.,** (2003) 4, S.C.C., 690. In addition to the above, he contended that the document in question, whether the indemnity or the guarantee could be invoked only after the determination of the liability of M/s. Pentagon, in appropriate legal proceedings. He has also relied on the Apex Court's decision in **Punjab National Bank Vs. Shri Vikram Cotton Mills & Anr.**, (1970), 1, S.C.C., 60 and **Union of India Vs. Raman Iron Foundry**, (1974) 2, S.C.C., 231. He further supported the judgment in all respects and prayed for the dismissal of the appeal.

10. Heard the respective learned counsel. The questions which are underlying in the appeal in question

are crystallized as follows - 1) Whether the document/deed (Exhibit-47) dated 4th September, 1985, executed by the respondents in favour of the appellant is a contract of indemnity or is a contract of guarantee.? - It is a contract of guarantee. 2) Whether appellant is entitled for an amount of Rs.34,00,000/-, with interest, as claimed, based on the said guarantee.? - Yes, with interest @ 14% p.a. 3) Whether the Suit was bad for non-joinder of necessary parties i.e. principal debtor M/s. Pentagon Engineering Pvt. Ltd.? - No. 4) What Order.? - Suit is decreed as per order in the appeal.

11. **ISSUE NO.1 :** The relevant Sections under the Contract Act are Section 124 and 126 which are reproduced thus:

> **"124. "Contract of indemnity" defined** - A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person, is called a "contract of indemnity."
>
> **126. 'Contract of guarantee', 'surety', 'principal debtor' and 'creditor'** - A 'contract of guarantee' is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the 'surety'; the person in respect of whose default the guarantee is given is called the 'principal debtor', and the person to whom the guarantee is given is

called the 'creditor'. A guarantee may be either oral or written.

12. The relevant clauses of the document/deed in question are as under:

IT IS FURTHER AGREED BY THE BANK AS FOLLOWS:

1. The liability of the Bank under this Guarantee in any event shall not exceed Rs,34,00,000/- (Rupees Thirty Four Lacs only).

2. The liability of the Banker under this guarantee shall not be impaired or discharged by any extension of time, or concession or indulgence allowed or granted by Mula Sahakari Sakhar Karkhana Ltd. to the Supplier.

3. Mula Sahakari Sakhar Karkhana Ltd. will be at liberty to make and effect changes in the said order without the Bank's consent provided that such changes do not have the effect to increase in burden and/or liability of the banker under this agreement.

4. This guarantee shall remain in force and ceases to have effect on expiry of 24 months covering the period from 4th September, 1985.

NOTWITHSTANDING anything herein before contained, our maximum liability under this guarantee is restricted to Rs.34,00,000/- (Rupees Thirty Four Lacs only). This guarantee shall remain in force upto 3rd September 1987 unless a suit of action to enforce claim under this guarantee is filed against us on or before 3rd September 1987 all your rights under this guarantee shall be forfeited and we shall be relieved and discharged from all liabilities hereunder."

There is no dispute that the document in question, as reproduced above, is the document based upon which the appellants claimed the amount of Rs.34,00,000/- by treating the said document as an unequivocal and unconditional Bank Guarantee. The Suit was filed as, inspite of invocation of the said Bank Guarantee, the respondents refused to honour the same by submitting that the said document was never intended or never instructed by the Company (M/s. Pentagon) to be a document of Bank Guarantee. It was throughout intended to be a contract of indemnity. There was no objection of any kind referred to or placed on the record by the appellants. The Officer of the Bank stated before the Court that the document in question was intended to be a contract of guarantee and not a contract of indemnity. The written document (Exhibit-46), as quoted above, lays emphasis on the preamble as under :

> "BEFORE THIS BANK GUARANTEE is made in favour of Mula Sahakari Sakhar Karkhana Ltd. by State Bank of India (Dombivli Industrial Estate Branch) agreed security the Sate Bank of India (Dombivli Industrial Estate Branch) hereby agrees and undertake subject to the terms and conditions set forth in this agreement to indemnify and keep indemnified Mula Sahakari Sakhar Karkhana Ltd. against all losses claims, damages actions and cost in respect of such sums which the Supplier shall become liable to pay as the terms of

the said order."

Therefore, in view of the above preamble, it is clear that by this document, respondents had agreed to indemnify and keep indemnified the appellants, against all losses, claims, damages, actions and costs in respect of such sums which the supplier shall become liable to pay as per the terms of the said order. The term "said order" here, as contended by the appellants, is nothing but the document in question. There is no dispute that the document in question was executed, based upon the agreement dated 25th September, 1983, for purchase of paper plant on turn-key basis with M/s. Pentagon Engineering Pvt. Ltd., the supplier. This document, therefore, as duly signed only by the respondent-Bank in favour of the appellants on 4th September, 1985, was accepted without any demur and, therefore, became final between the appellants and the respondents, including the terms and conditions agreed to in the document irrespective of the clauses of the main agreement dated 25th September, 1983.

13. As M/s. Pentagon Engineering Pvt. Ltd. had proposed and as the appellants had agreed, the condition of 10% retention was waived and it was agreed by letter dated 6th April, 1985, to provide the Bank Guarantee of

the said 10% amount. The preamble of the document in question creates an impression that the said document is a contract of indemnity and not a contract of guarantee.

14. It is well settled, and, as rightly observed by the learned Judge, that the oral evidence cannot prevail over the written and agreed document. This document remained unchallenged till the invocation of the Bank Guarantee in question. The subsequent document and oral evidence, therefore, in the facts and circumstances of the case, cannot prevail over the clauses of the written document in question (Exhibit-46).

15. In this background, the respondents, by their letter dated 13th August, 1987 (Exhibit-58), in reply to the appellants letter dated 4th September, 1985, of invoking the alleged Bank Guarantee in question, informed as under:

> "The true facts are that we had at the request of Pentagon Engineering Pvt. Ltd., executed on 4th September, 1985 an agreement of indemnity for Rs.34 lacs thereby indemnifying you against all losses, claims, damages actions and costs which you may suffer as a result of payment by you of the sum of Rs.34 lacs, in accordance with the terms of the Agreement; entered into by you with the Pentagon Engineering Pvt. Ltd., on

> 25th September 1983. It was, we are advised, never the intention that the indemnity given by us should cover all your claims against the said Company. The recital in the said Agreement dated 4th September, 1985 restricts the scope of the indemnity to cover your claim in respect of final payment of Rs.34 lacs in connection with the design, performances, workmanship and against defective materials of the equipments supplied to you."
>
> "Unless and until the claims disputes and differences between you and the company are adjudicated upon and determined by competent court or authority and until is established that you have in fact suffered any loss or damage for design, performance, workmanship or against defective materials, the question of our making any payment to you does not arise. Your claim is premature and not maintainable in law. We, therefore, regret our inability to make any payment, which please note."

16. In view of the provision of Section 91 of the Evidence Act, the oral evidence cannot be utilised to disconnect the surrounding circumstances and or object and intention to interpret a document. There is no bar for resorting to external aids to interpret any writing in case of conflict or confusion or uncertainty, but not otherwise. In our view, the wordings in the document in question are clear and unambiguous and as the document in question remained unchallenged till the invocation of the Bank Guarantee, the intrinsic oral evidence or earlier correspondence, executed between the appellants and the company cannot be resorted to, to bring in the

intention of the document as sought to be contended by the respondents by treating the said document as a contract of indemnity and not a Bank Guarantee.

17. The learned Judge has considered the Apex Court judgments in **Bhaskar Waman Joshi Vs. Shrinarayan Rambilas Agarwal (deceased) & Ors.**, AIR 1960, S.C., 301; **Ramkishorelal Vs. Kamalnarayan**, AIR 1963, S.C., 890; **S. Chattanatha Karayalar Vs. The Central Bank of India Ltd. & Ors.**, AIR 1965, S.C., 1856; **P.L. Bapuswami Vs. N. Pattay Gounder**, reported in AIR 1966, S.C. 902; **Sundaram Finance Ltd. Vs. State of Kerala**, AIR 1966, S.C., 1178; **Modi Co. Vs. Union of India**, AIR 1969, S.C., 9; and, **The Godhra Electricity Co. Ltd. & Anr. Vs. The State of Gujarat & Anr.**, AIR 1975, S.C., 32, in support of his reasoning that an agreement has to be interpreted as a whole by giving natural meaning to the words used therein. A contract cannot be interpreted in abstract as a legal doctrine, but it has to be interpreted in relation to the realities of the situation in which it is entered into. The surrounding circumstances, therefore, permissible to look into. The external aids in interpretation could be resorted to if there are ambiguities and in such case, even subsequent interparties document, statements and conduct may be useful and relevant.

18. After scanning, we noted that the Managing Director of the appellants PW1-Vinayak deposed in support of their pleading that as per clause 15.2.4 and 15.2.5 of the agreement the company was to retain 10% of the contract value and that comes to Rs.34,00,000/-. He further deposed that there was no provision in the original agreement to pay this amount of Rs.34,00,000/- after taking Bank Guarantee before the plaint was commissioned. The covering letter dated 7th September, 1985, with the Bank Guarantee in question executed by the respondents was received by one Prabhu at their factory at Sonai on 7th September, 1985, based on which, the amount was paid by the demand draft. There was no format of the Bank Guarantee stipulated. They had accepted the Bank Guarantee without any demur or objection, as it was found to be correct. He further deposed that the document (Exh.46) was furnished after considering the agreement dated 25th September, 1983, and the same was a Bank Guarantee and not an indemnity bond. He deposed that the Bank Guarantee was not restricted to 10% amount, but it was comprehensive and was enforceable before 8th September, 1987. M/s. Pentagon could not have received this 10% amount in absence of the said Bank Guarantee. The Bank Guarantee covers everything. However, he was unable to give the

details of the amount payable to M/s. Pentagon out of the 10% amount to be retained. He deposed that they invoked the Bank Guarantee on 27th July, 1987. M/s. Pentagon had nothing to do with the Bank Guarantee as the agreement was between the Bank and the appellants-plaintiffs. The dispute between the plaintiffs and M/s. Pentagon was in no way concerned with the bank. He has, therefore, deposed that the Guarantee did not provide for only the balance due after adjusting claims of M/s. Pentagon but it is only for claims against M/s. Pentagon. Therefore, while invoking the Bank Guarantee they had made the respondents aware that more than Rs.34,00,000/- were recoverable from M/s. Pentagon. Therefore, M/s. Pentagon could not instruct the Bank not to pay. In the cross-examination, he admitted that "Exhibit-46 does not bear endorsement about the person who brought it to us or the inward number. They have not asked the respondent-Bank why they furnished the Bank Guarantee without having asked by them. He further admitted that "Bank Guarantee Exhibit-46 is not concerning clause 17.3". He denied the suggestion that the claim against the defendants was improper, premature and contradictory to Exhibit-46."

19. Another witness of the appellant, PW2, Tukaram

who was a permanent employee of the appellants and, at the relevant time, was the Chief Accountant, deposed about the monetary transaction with M/s. Pentagon. However, nothing was deposed about the nature of the document in question, except existence of Exhibit-46.

20. Another witness PW3 Anant Rane was also unable to throw much light on the nature of the document Exhibit-46 in question as to whether it was a Bank Guarantee or it was a contract of indemnity.

21. The last witness PW4 Mohammed Patel, who served with the appellants-plaintiffs as an Accountant has referred to monetary transactions and supporting extract of accounts to show the amount actually paid to M/s. Pentagon and nothing more than that. Therefore, except PW1, was able to support the case of the appellants-plaintiffs that the document in question was intended or in fact was a Bank Guarantee and not a contract of indemnity. We have noted that the appellants had never objected to the nature and the contents of the said document Exhibit-46 inspite of the rest of the same. There was no correspondence on the record to show any such objection. There was no fixed format of the Bank Guarantee. There was no objection raised when the said document was furnished by the

respondents even though it was not called for. The appellants and M/s. Pentagon had in fact had acted upon the said document immediately. The said witness was unable to explain the meaning of the word "comprehensive" as referred in the policy copy. He agreed in paragraph 41 of his examination that the Bank Guarantee was with an intention to take over all the losses that might be caused on account of Ms. Pentagon failing to perform supplying effective machinery etc. There remained undisputed position that the appellant had not obtained any decree of award against M/s. Pentagon in respect of the loss caused, if any. The said witness was also unable to give any reason for not joining M/s. Pentagon as a party though the document in question concerned loss caused on account of M/s. Pentagon. This part of the cross-examination, according to us, in no way disturbs the case of the appellants about the intention of creating a Bank Guarantee.

22. The learned Advocate appearing for the appellants further pointed out that even the respondents' witness D.W.1 Shankar Keskar admitted that the document in question (Exhibit-46) was intended and was in fact a Bank Guarantee and not a contract of indemnity. He deposed that - "The document is a Guarantee for performance, workmanship, design and

against defective material supplied by M/s. Pentagon to the plaintiffs. The Guarantee was furnished for realising final payment to M/s. Pentagon. I signed the document. The document does not bear the signature of any one else." In the cross-examination, however, he has admitted that Exhibit-46 does not show that it was executed in the form sanctioned by the Head Office, but as per the sanction of the Head Office. He deposed that Exhibit-46 was executed for a special purpose. It provides a special Guarantee and the liability of the State Bank was restricted to Rs.34,00,000/- and the word "Guarantee" was used ten times. Nowhere the word "indemnity bond" was used. He deposed that - "The document was executed as a Bank Guarantee and was intended to be accepted by the plaintiffs as a Bank Guarantee. Exhibit-46 is an agreement between the plaintiffs and the State Bank, but it is a tripartite agreement. It is a contract to discharge liability. Exhibit-46 is a subsidiary auxiliary and accessory to the main contract between the plaintiffs and M/s. Pentagon. Exhibit-46 presupposes some contract for transaction as principal duty. Exhibit-46 is not an original or independent contract. Exhibit-46 is a promise to the plaintiffs to whom M/s. Pentagon is answerable. The Bank has accepted limited responsibility for performance of the owners by M/s.

Pentagon to the plaintiffs under the original agreement. He agreed that they had not assumed any original or independent obligation by Exhibit-46. He further deposed that the words "an agreement for purchase on turn-key basis" were used in Exhibit-46 blindly. He further deposed that - "Likewise, I referred to the terms of the contract between plaintiffs and Pentagon in paragraph 20 of Exhibit-46 also blindly." He admitted that he had never seen the agreement between the plaintiffs and Pentagon. He has, however, deposed that the application for the Bank Guarantee was addressed to his Branch and accordingly, the Bank Guarantee was issued. He deposed that by Exhibit-46, the Bank has two sureties for the obligation to be performed by Pentagon and the said document is of surety and not security. He further deposed that in Exhibit-46 "We have permitted Pentagon and the plaintiffs to make changes, grant concession or indulgences in their agreement. He deposed further that :

> "4. In para 1 of page 2, of Exh.46, we have by way of bank guarantee agreed to indemnify the plaintiff and also to keep them indemnified. We have guaranteed for all losses caused to plaintiff by Pentagon, all claims of plaintiff against Pentagon, all damages caused to plaintiff by Pentagon and all actions of Pentagon resulting in losses, damages to plaintiffs and all claims against plaintiff. The guarantee is furnished for

> all losses, claims, costs, damages of plaintiff from Pentagon. Exh.46 does not include or consider claims of Pentagon from the plaintiff. There is no condition other than limit of Rs.34,00,000, in Exh.46 to comply with the demand of plaintiff. The only term about payment is that plaintiff should invoke the guarantee before 3rd Sept., 1987. Exh.46 also provides that if we failed to honour the guarantee, the bank along would be sued before 3rd Sept., 1987."

He deposed that "It is true that the Guarantee is not executed for the amount found due after considering the claims and counter claims between the plaintiffs and Pentagon. It is executed only for the plaintiff’s claim against Pentagon".

23. The document, Exhibit-46, is supported by the evidence of DW1 who is the witness of the respondent-Bank. This witness has supported the written agreement which was signed and acted upon by the concerned parties, without any objection at the relevant time and treated the same as Bank Guarantee.

24. Another witness of the respondents DW2 Shri Bal Vasaikar supported to the extent that the company Pentagon has suggested to waive the Bank Guarantee and based upon that, a format was handed over to the respondent-Bank. Nothing much was extracted from this witness insofar as to the interpretation of the document

in question.

25. The third witness of the respondent-Bank, DW3, Vijay Gadkari, who was working as a Manager of the Bank, Palghar Branch, has deposed as under :

> "The Branch Manager has forwarded three proposals on behalf of Pengaton. Alongwith this letter the draft of indemnity to be executed by the bank was submitted. The proposal was recommended by the Br. Manager for the purpose mentioned in the remarks column. In column No.5 the Br. Manager mentioned performance guarantee. The documents executed by a bank are classified as letters of credit and bank guarantee. Under category bank guarantee we include bank guarantee bonds, surety. The category recommended, contemplated or sanctioned did not include an unconditional obligation to pay on demand."

Based on the application/letter received dated 19th June, 1985, he has further deposed as follows :

> "We sanction an unconditional bank guarantee only against 100% cash margin with us even such guarantee was asked for in this case, we would not have sanctioned it. Vide exh.333 the proposal was sanctioned, and consent was conveyed to the bank, against 10% margin. Exh.46 is the document requested for recommended, approved and sanctioned. The plaintiff could institute a suit on Exh.46 after invoking the bank guarantee under the circumstances mention in Exh.46."

This witness has supported the respondents' case that Pentagon should have been made a party. In the cross-examination he has further answered : "Nobody has instructed me in writing that indemnity should be called guarantee". He agreed that Exhibit-46 was executed on a stamp and an agreement is a guarantee. He further deposed in the cross-examination that from the accounts, it was not possible to decide whether Exhibit-46 is an indemnity bond or a guarantee. He further deposed that the Bank did not had a standard form of a Bank Guarantee. However, in the cross-examination, he stated - "It is true that we treated Exhibit-46 and executed it as a Bank Guarantee because we wanted to oblige our clients Pentagon, who wanted a Bank Guarantee. The Bank did not have any malafide intention while executing Exhibit-46. We wanted to believe genuinely that Exhibit-46 is a Bank Guarantee."

26. We have gone through the evidence, as well as, the documents referred and relied upon. We have also gone through the document (Exhibit-46) in question and, after scrutiny, we are of the view that there are no serious ambiguities in the document.

27. In the present case, after going through the evidence of PW1, DW1 and DW2, read with the documents and correspondence prior to the execution of the Deed (Exhibit-46) in question, we are convinced that Exhibit-46 has a basic ingredient of a Bank Guarantee and it is not a contract of indemnity. The testimony of these witnesses, in no way, derogates the document in question. On the contrary, the evidence supports the purpose and object of the execution of the Bank Guarantee in question. It also supports that the parties, specially the appellants are the creditors-beneficiaries, the respondents-Bank are the guarantors-the surety and the supplier is M/s. Pentagon - the principal debtor. As we have noted and as contemplated under Section 124 of the Contract Act, such Bank Guarantee should have three basic ingredients i.e. creditor, guarantor and principal debtor. On a bare reading of this document, it is nothing but a tripartite agreement between the parties. M/s. Pentagon submitted the said Bank Guarantee by it’s letter dated 7th September 1985 to the appellants. The appellants, as noted above, without any demur or objection, accepted this document as a Bank Guarantee and based upon the same, the amount was released. There is a evidence to support that in absence of this Bank Guarantee, the amount would not have been released by the appellants.

28. We have also noted that the words "Bank Guarantee" and "Guarantee" have been used in the said document for more than six times. The preamble of the said document itself mentions the words "This Bank Guarantee". The latter part of the preamble, however, refers to the words "indemnity" and "keep indemnified", but the rest of the clauses reflect the word "guarantee" only.

29. We have also noted that there was no reference to the concept or contract of indemnity in any of the earlier document or the main agreement between the appellants and the supplier M/s. Pentagon. There was no intention at any point of time between the parties to execute any contract of indemnity. There is ample evidence on the record to support that the intention was to execute a Bank Guarantee. The preamble clause only reflects, endorses and indemnifies the liability to pay all claims arising out of the contract in question. The intention was to keep indemnified the appellants against all losses, claims, damages, actions and costs in respect of sums which Pentagon should become liable to pay as per the terms of the main contract. As noted above, the words "said order" is in reference to the Bank Guarantee in question. In the present case, the

claim of the appellant was more than the amount referred in the Bank Guarantee in question i.e. Rs.34,00,000/-. The said claim was quantified in the Notice. As the Bank Guarantee was restricted to Rs.34,00,000/-, the present action was initiated after invoking the said Bank Guarantee by the appellant. The appellant restricted themselves to the said claim only. Therefore, there was no question of making payment by the bank of all the losses or claims or liability as raised, or about to settle through the disputes pending between the appellant and Pentagon. Therefore, merely because the document in question is loosely worded and is not the fixed format of a Bank Guarantee, it is not acceptable that the document in question is not a Bank Guarantee or that it is a contract of indemnity.

30. The Apex Court in **Punjab National Bank Vs. Shri Vikram Cotton Mills Ltd.** (supra). While dealing with a case of falling under the ambit of Section 124 and 126 of the Indian Contract Act observed as under:

> "9. Section 124 of the Indian Contract Act defines a "contract of indemnity". A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person, is called a "contract of indemnity". Section 126 defines a "contract of guarantee". It states:

> "A 'contract of guarantee' is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is given is called the 'surety' : the person in respect of whose default the guarantee is given is called the 'principal debtor', and the person to whom the guarantee is given is called the 'creditor'. A guarantee may be either oral or written."
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> 10. A promise to be primarily and independently liable for another person's conduct may amount to a contract of indemnity. A contract of guarantee requires concurrence of three persons - the principal debtor, the surety and the creditor - the surety undertaking an obligation at the request express or implied of the principal debtor. The obligation of the surety depends substantially on the principal debtor's default; under a contract of indemnity liability arises from loss caused to the promise by the conduct of the promisor himself or by the conduct of another person."

In the present case also, the document in question was executed by the respondents-Bank and the appellants-plaintiffs. The supplier-Pentagon was not the party to the said document. As already noted, the supplier, by its letter had submitted the bank Guarantee to the appellants and the parties were acted upon the same accordingly.

31. The respondents-Bank, in its reply dated 13th August, 1987, to the invocation by the appellant by

letter dated 10th August, 1987, resisted the whole claim of the appellants, which was never demanded by the appellants, from the Bank. The Notice itself reflects a total demand of Rs.34,00,000/- based upon the agreement of the Bank Guarantee in question and not more than that. In view of this, we are of the view that there was no question of settlement of any dispute or differences about the exact amount between the appellant and the supplier-Pentagon. The supplier-Pentagon was not the signatory to the Bank Guarantee given by the respondent-Bank to the appellant at their instance. It is not the case that M/s. Pentagon had never instructed or executed or submitted the Bank Guarantee in question to the appellant. There is no case of any fraud or misrepresentation. The document, as well as, the intention between the parties was clear to cover the comprehensive claim of the appellant restricted to the extent of Rs.34,00,000/-. Therefore, in our view, after invocation, the respondent-Bank ought to have honoured the same. The learned Judge, therefore, according to us, was wrong in overlooking the supporting evidence of PW1, DW1 and DW2, which remained undisturbed even in the cross-examination.

32. We find that upon its true construction and taking the document as a whole, read with the

surrounding circumstances and corresponding and connected documents, it is clearly a document of Guarantee and not a document of indemnity as sought to be contended by the respondent and as held by the learned Judge. Therefore, according to us, the express terms of the written agreement in question, supported by the testimony of the respondent-Bank's Officer itself, apart from the appellants, some statements in the cross-examination or raising doubts about the nature of the agreement by one of the Bank witness, that itself would not affect the written agreement in question. As per Section 91 and 92 of the Evidence Act, 1872, no evidence dehors the terms of the agreement, whether documentary or oral, can be led by the parties to get out of the express terms thereof as observed by the Apex Court in the case of **New India Assurance Co. Ltd.** (supra).

33. The principal debtor, according to us, in view of this background and the agreement, is bound to fulfill its obligation flowing from the contract, based on the main contract itself.

34. We are not convinced with the submission raised by the respondent-Bank and as held by the trial Court that the document in question was in the nature of

a contract of indemnity and not a contract of guarantee. In view of the unequivocal condition of the contract in question and as the amount is already ascertained and fixed by the parties so far as the liability claim is concerned, to the extent of Rs.34,00,000/-, we are of the view that there is no question of settlement of any dispute or conflict insofar as any claim between the appellant and M/s. Pentagon. Respondents had no concern with the said dispute, if any, at this stage once the Bank Guarantee in question was invoked within the prescribed time as per the terms and conditions. The respondents had no option, but to honour the same. The document in question is not a contract of indemnity and in view of the above reasoning, it is a Bank Guarantee and, therefore, there is no question that the appellants should prove the actual loss before filing any claim. The present Suit, therefore, cannot be treated as a Suit based on the contract of indemnity. It is a Suit for the enforcement of the Bank Guarantee. It is also clear from the provisions of Section 126 of the Contract Act read with the other provisions that the term "liability" and "deed" as referred under the Section means and includes present deed or liability or future deed or liability. In the present case, there is an existence of an element of promise and obligation. As the principal debtor failed to fulfill its liability,

the surety-respondent Bank are under an obligation to honour the Bank Guarantee. The very object of the Bank Guarantee would be frustrated if the appellants-creditor are required to wait for the settlement of the future amount or damages against the principal debtor M/s. Pentagon. The appellants are entitled to their claimed money without any delay or demur. The nature and need of such commercial contracts and documents need to be respected by the parties concerned. There is no case of any fraud or irretrievable injustice or harm. The respondents' liability is not discharged by any means. The Bank Guarantee in question, at the most, can be said to be performance guarantee, but it cannot be, in any sense, treated as a contract of indemnity.

35. **ISSUE NOS.3 & 4:** In view of the above, we are of the view that the learned Judge is wrong in holding that M/s. Pentagon was a necessary party. As observed above, if the document in question is a Bank Guarantee, then the principal debtor is not a necessary party in such Suit. The respondent-Bank is bound by the terms and conditions of the Bank Guarantee to honour the said document and make the payment to the appellants, as claimed. In view of the above reasoning, we are of the view that the principal debtor M/s. Pentagon was not a necessary party. The document Exhibit-46, is not an

independent contract like a contract of indemnity. It is a tripartite agreement. As the appellant need not prove losses caused by the beneficiary, M/s. Pentagon therefore, is not a necessary party even though the main agreement dated 25th September, 1983, was between M/s. Pentagon and the appellant. In view of the clear terms of the document, the liability of the supplier M/s. Pentagon , in view of the default and invocation of the Bank Guarantee, need no further evidence to prove any loss. The comprehensive amount of Rs.34,00,000/- as claimed had been crystallized by the parties. Therefore, the learned Judge was wrong in dismissing the Suit for non-joinder of party.

36. The important aspect in the present case is the construction and interpretation of the document in question. The extrinsic evidence of the factual situation is essential for the purpose of construing the document in its context. In the present case, the words "indemnity" and "indemnification" have been used in the preamble, based upon which, the respondent sought to contend that this document is nothing, but a contract of indemnity. The recital in the preamble in question itself cannot be the foundation to interpret the document in question as a document of indemnity. In the facts and circumstances of the case, all essential

characteristics of a contract of guarantee are present. It includes a guarantor, creditor, principal debtor, a written document, ascertained liability, nature of obligation guaranteed, limitation, period of invocation and claim, debtor's default and the clause when guarantor's liability arises. The requirement of issuing or invoking the Bank Guarantee and the duration of the Bank Guarantee are also available in those clauses. The appellants are, therefore, entitled to enforce the said Bank Guarantee as per the arrangement between the parties as guarantor's rights have been created, based upon the relationship and the guarantor, therefore, is required to honour the said Bank Guarantee once demanded by the creditor like the appellants in the present case. After going through the evidence and the document in question, it is not possible to accept that the parties have agreed or intended to keep the appellants indemnified against loss only and that too, after ascertaining and/or settlement of disputes between the parties. The evidence shows that the intention was to submit the Bank Guarantee and based upon which, the supplier-Pentagon and the appellant acted without any objection.

37. The document in question if taken note of, referred to the main agreement between the parties dated

25th September, 1983, wherein a specific amount has been agreed. The Guarantee became effective the moment the principal debtor failed to perform its obligation and as appellants invoked and demanded to perform the same. The promise to perform was a condition precedent and the respondents were liable to make the payment as the principal debtor committed the default of their obligations as demanded by the appellants. In this background, we cannot overlook the circumstances under which the particular words were used and/or misused. If we read the document harmoniously, we are convinced that the document in question is a contract of guarantee and not a contract of indemnity.

38. After going through the Bank Guarantee and the related evidence in support of the same, it is difficult to accept the contentions raised by the respondent-Bank that the said Bank Guarantee was not absolute and unconditional, but it was a conditional one. It is also not accepted that the Bank Guarantee in question was to cover the final payments to be effected by the appellant-plaintiff to M/s. Pentagon. It is very clear from the record that the Bank Guarantee in question was basically for the performance of the contract and admittedly, for whatever may be the reason, there were delays and unsatisfactory and non satisfactory

performance. In this background, there was no question of ascertaining any amount, as admittedly as per the main contract M/s. Pentagon failed to perform its obligations and being a secondary and supplementary agreement in question arising out of the main contract, there remained no doubt that the parties are bound to honour the said document and, in the result, the claim as raised by the appellant-plaintiff arising out of the same was contract and within the framework of the said Bank Guarantee. Therefore, the reliance on AIR 2000, Bom. 405 and (1999) 8, S.C.C., 438, is not applicable and are distinguishable on the facts itself. There is no case of any injunction against encashment and any case of fraud or irretrievable injury or harm in the present case. The principle regarding the Bank Guarantee and connected aspects as dealt with in **Daewoo Motors** and **Hindusthan Construction Company** (supra) by the Apex Court, in a way, supports the case of the appellants.

39. If the terms and conditions of the Bank Guarantee are unconditional and absolute, the respondents have no choice but to honour the same. The Bank Guarantee, therefore, if read alongwith the terms of the original contract between the parties, there remains no doubt that the Bank Guarantee in question was

absolute and unconditional. Therefore, the invocation of the Bank Guarantee and the demand as raised and the filing of the present suit cannot be said to be premature or unjustified. In this background, the contention of the respondent-Bank that this document in question whether is an indemnity or a guarantee could had been invoked only after the determination of the liability of M/s. Pentagon in appropriate legal proceedings, cannot be accepted. The reliance on the Apex Court's judgment in **Punjab National Bank** (supra) in the facts and circumstances of the case, is not helpful to the respondents. There was no question involved in that case about the interpretation of such document as to whether it is an indemnity or guarantee. On the facts of the present case itself, based upon the surrounding circumstances, the evidence led by the parties and specially the respondent-Bank itself, we are of the view that there is sufficient material on the record to show that the document in question is nothing, but a Bank Guarantee and it was never intended to be a contract of indemnity.

40. In the present case, respondent-Bank had agreed to all the losses arising out of the main agreement dated 25th September, 1983, to the extent of Rs.34,00,000/-. There is a sufficient material on the

record to show that the actual losses as per Notice dated 7th September, 1985, was more than Rs.34,00,000/-. However, in view of this Bank Guarantee, the amount was restricted only to Rs.34,00,000/- and accordingly, the Suit was filed after invoking the Bank Guarantee. Therefore, according to us, there is no question of settlement of any pecuniary liability between the parties as sought to be contended. In the facts and circumstances of the present case, the amount, if ascertained to the extent of Rs.34,00,000/- need no further settlement or assessment. The assessment of the loss, as sought to be contended and as discussed by the learned Judge in paragraphs 78 to 83 of the judgment is not correct. The assessment of losses as referred and dealt with by the learned Judge on the basis of Issue No.6, therefore, is not correct. There is no question of assessing the losses of the appellant at this stage in view of the above reasoning and in view of the agreed Bank Guarantee amount of Rs.34,00,000/-. There is no question of any loss to the appellant to be assessed at this stage on account of payment made as a consequence of the respondents-Bank furnishing Exhibit-46. Appellants, according to us, need not prove any loss in view of the clear terms and conditions referred in the Bank Guarantee. Therefore, issue No.6 was also decided wrongly by the learned Judge.

41. In the present case, the appellants-plaintiffs have claimed interest @ 18% p.a.. The observation in paragraph 93 by the learned Judge is sufficient to grant the interest @ 14% p.a. and not @ 18% p.a., as claimed. The said paragraph 93 is reproduced below:

> "93. The plaintiff has claimed interest at the rate of 18% per annum. The plaintiff has tendered statements of accounts of interest paid on loans and deposits. These statements are at Exhs. 145 to 150. P.W.1, Managing Director of plaintiff Shri Ambre, has admitted in his deposition Exh. 107 in para 25, that plaintiff is required to pay interest at 12% to 14 1/2% with quarterly rests. He admitted that interest at the rate of 18% per annum was not paid by plaintiff to anyone though plaintiffs' claimed to have recovered interest at that rate. Interest cannot be claimed by way of penalty. Interest could only be claimed to compensate the party for the probable loss. As interest has not been paid at the rate 18% per annum, plaintiff would not be entitled to recover interest at this rate. At the most, plaintiff may be entitled to interest at 14% per annum which is maximum rate at which the plaintiff had paid the interest to others. This issue is answered thus: at 14% per annum if at all."

42. In view of the above reasoning, the Appeal is allowed and the Suit is decreed as follows:

(a) The respondents are ordered to pay

Rs.34,00,000/- (Rs. Thirty Four Lacs only) under the invoked impugned Bank Guarantee together with interest of Rs.51000/- (Rupees Fifty one thousand.)

(b) The respondents are further ordered to pay interest at the rate of 14% at quarterly rests from the date of invocation of the impugned Bank Guarantee.

(c) No order as to costs.

[R.M.S. KHANDEPARKAR, J.]

[ANOOP V. MOHTA, J.]

[srpasha@hc]